

# Yours, Mine & Ours: Ethical Landmines in Representing Spouses in Blended or Stepfamilies

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# Agenda

# Agenda

- ***What is a blended family***; common forms of blended families. Clarifying the blended family makeup. Some statistics on how common blended families are in practice.
- ***Working effectively with blended families***: Should it be joint or separate representation? What might you include in your retainer agreement or a side agreement about representation? What signs to look for to protect the client and yourself?
- How to properly prepare for the ***initial meeting*** – Are your questionnaires and other forms updated to reflect blended family data? How to engage and move forward.



# Agenda (cont.)

- ***Conflicts of interest***: Sources of common conflicts of interest. Efficacy and advisability of obtaining waivers of conflicts of interest. Distinction between ***consentable*** and non-***consentable*** conflicts.
- ***Specific practical estate planning situations*** that can present ethical challenges, including marriage contracts, joint tenancy, gift-splitting, gift tax returns, etc. And much more!!!
- ***Two actual reported decisions*** that illustrate practical and ethical quagmires that estate planners who work with blended family couples blended families face.

Who  
*IS*  
The **Bl**ended**ED** Family?

- Blended/stepfamily couples-since the 2010 U.S. Census, this has been the most common form of relationship. The 2020 U.S. Census reconfirmed this.
- Same sex partners, including married, unmarried and those in civil unions.
- Unmarried couples-fastest growing demographic segment of the population

# Blended v. Step?

- While we often use the term “blended” to describe familial organizations where the romantic partners don’t share all the children in the organization, you should first understand that some experts who work with or research so-called “blended families” vehemently object to the use of the term “blended,” as many of these familial organizations are anything but “blended” as the meaning of that term is commonly understood.
- But those who strongly prefer the term “blended” view this as aspirational for every such family.
- Consequently, many only use the term “step,” while others only use the term “blended,” but, for our purposes, the terms “blended” and “step” are synonymous, and we, though sensitive to the objections of all concerned, use them interchangeably.

# Definition of “Blended/Step-Family”

At least

one partner has

at least one child

who is not child of

the other partner.

# Statistics Clarifying the “Blended Family”

## Blended Family Statistics:

- 62% of married/cohabiting couples under age 55 that have at least one living parent, the couple member and at least one adult child have at least one step-kin relationship in the three generations.
- 1,300 new stepfamilies are formed every day.
- 65% of remarriages involve children from a prior marriage on at least one side, creating a blending family.
- 40% of married couples with children (i.e., families) in the US are step-couples (at least one partner had a child from a previous relationship before marriage; this includes full and part-time residential stepfamilies and those with children under and/or over the age of 18).
- An estimated 113.6 million Americans have a step-relationship.
- Sources: <http://www.smartstepfamilies.com/view/statistics>;  
<http://brandongaille.com/20-noteworthy-statistics-of-blended-families/>

# Statistics Clarifying the “Blended Family” (cont.)

## Blended Family Statistics:

- Approximately one-third of all weddings in America today form stepfamilies (demographic estimate, Deal). This includes first marriages - 15% of *first* marriages create stepfamilies.
- A national Pew Center report (Livingston, 2014) finds that 40% of all new marriages in the US are remarriages for one or both of the partners.
- 42% of adults (102 million) have a step-relationship (either a stepparent, a step or half sibling, or a stepchild).
- One-third of individuals who got divorced in 2008 were re-divorcing, that is, divorcing again.
- And, of new marriages, 40% are remarriages (20% for one partner, 20% for both partners).
- Sources: <http://www.smartstepfamilies.com/view/statistics>; <http://brandongaille.com/20-noteworthy-statistics-of-blended-families/>

- Each Family is **Different**.
- Each Situation Requires Different Approach.
- The following slides review archetype relationships.



# Lies, Damn Lies and Statistics

- The average length of a **first** marriage that ends in divorce is roughly eight years—7.8 years for men, 7.9 for women.
- Moving into **second** marriages that end in divorce, the median length of a marriage shortens a bit, i.e., for men is 7.3 years, while for women, it drops to 6.8 years.
- There are two more sobering statistics that estate planners must keep in mind when considering irrevocable lifetime estate planning advice for blended family couple clients:
  - 60% of second unions end in divorce.
  - 74% of third unions fail.
- Estate planners must be both aware of and circumspect about the undeniable reality of these statistics, particularly for the blended family couple.

**Brady Bunch:**  
Widow and Widower  
Both in 40's,  
Each with three minor children  
from prior marriages.

**May-December Romance:**  
Wealthy Widower-80  
3 Adult Children in their 50s,  
Marries Woman-26  
Who has a 7-Year-Old Daughter.

# **Empty Nesters:**

Widower – 72

Has Pension, Received Late Wife's Insurance

3 Adult Children

Marries

Divorced Woman – 72

3 Adult Children

No Assets Except Home

No Income Except Social Security.

# **Eat, Drink and Remarry:**

63-Year-Old

One son

Large alimony obligations

3 Prior Marriages

marries

35-Year-Old

Two-time divorcee

Two dependent minor sons.

# **Same Sex Blended Family:**

46-Year-Old Woman

Marries

37-Year-Old Woman

Both are Parents

One Divorced with 10-Year-Old

One with Adopted Son – 18.

# **Yours, Mine and Ours:**

Man Age 43

Divorced

Marries

Woman Age 41

Each - Minor Child

Each - Joint Custody

Together – 7- and 3-Year Olds.

# Methods of Representation- Choose Wisely and Defensively

Document in writing what the clients were told about the express method of representation.



# Methods of Representation

- Assuming that you're comfortable enough to represent a couple in a blended family, how may you represent a couple?
- **Jointly**—where you won't keep secrets between the partners.
- **Separately**—where you treat each partner's secrets as if he or she was a separate client. Be careful!
- The 4<sup>th</sup> Ed. of the *ACTEC Commentaries on the Model Rules of Professional Conduct* (2006) contained the following statement “***some experienced estate planners regularly undertake to represent husbands and wives as separate clients.***”
- Interestingly, the above highlighted statement was removed in the 5<sup>th</sup> Ed. of the *ACTEC Commentaries on the Model Rules of Professional Conduct* (2016), suggesting a ***retreat*** on the efficacy or advisability of treating each spouse as ***separate*** clients of the lawyer when the same lawyer represents ***both spouses***.

- Some conservative lawyers **won't** represent a **couple** in blended family (will **only** represent one partner). However, many will do so, especially if the couple is married and insist.
- We suspect, but could not find supporting data, that most lawyers will jointly represent a couple who comes to them as a married joint client.
- ***Shouldn't proper focus be on what is best for client?***  
(We maintain answer is "YES!")
- Looking out for client is in estate planner's **long-term** best interest too:  
(**Happy** clients pay and refer others;  
**unhappy** clients more likely to **sue**,  
less likely to **pay** and  
very likely to **tell others** about bad experience)

## Benefits of joint representation:

- ***Cost savings*** (only one set of estate planners).
- Efficiency and ***synergies of effort***.
- Better ***communication*** between partners/spouses.
- Being treated as ***partners***, not adversaries.
- Planning is often ***integrated***.

**But...There are also some potential downsides to joint representation that can't be safely ignored or minimized.**

- Perhaps the best illustration is where the spouses' interests aren't *identical* and can't safely be treated as identical.
- One very important example involves federal gift tax returns and *separate* per person transfer tax applicable exclusion amounts (portability helps only if the couple *dies while married*), and each spouse must prepare and sign *separate* federal gift tax returns, since there's no *joint* gift tax return.

## Benefits of true separate representation (as opposed to the same lawyer's simultaneous separate representation of each spouse):

- Undivided attention and ***loyalty*** of estate planner.
- Total ***freedom to say*** what client feels and wants to have done.
- Lower chance of estate plan ***challenges***.
- ***Note:*** Doesn't eliminate challenges by surviving partner or partner's children. See *Sindell v. Gibson, Dunn & Crutcher, infra*.

## Signposts of need for *Separate* Representation (Despite what they *say* that they want)

- One partner is ***childless*** (partners usually have different loyalties), but the other is not.
- One partner ***does all the talking*** or seems to exert ***control*** over the other.
- ***Short*** length of relationship.
- ***Number*** of past relationships.
- Significant ***age disparity***.

## Signposts of need for *Separate* Representation (Despite what they *say* that they want (cont.)):

- Significant disparity in ***wealth or income***.
- ***Economic dependence*** of one partner on the other (whether or not used against him/her).
- ***Existence*** of marriage contract or property agreement.
- ***Information*** held by one partner ***off-limits*** to other partner, *e.g.*, a secret, etc.

Many prospects for potential conflicts of interest when drafting wills or trusts or other aspects of the planning

- ***Major Issue: interpretation*** of marriage contract or property agreement.
- ***Major Issue:*** How partners have maintained or should maintain ***separateness*** of property, i.e., not commingled separate property.



## Potential Conflicts of Interest When Drafting Wills or Trusts or Other Aspects of the Planning

- Right of partner in property of other partner in areas such as “equitable interest” or “quasi-community property.”
- Keeping client *confidences*.
- Any *non-reciprocal* will or trust provision that adversely impacts one client’s freedoms to act or rights:
- **Example:** One partner appoints other to serve as fiduciary while the other partner chooses someone *other* than his or her partner.

## Bottom line:

- Practice *defensively* because modern family estate planning can be treacherous waters where storms can come up instantly and without warning!
- For example, the recent *Wellin* malpractice case, *Wellin v. Farace*, No. 20-1120 (unpublished 4th Cir. 2021). If you become aware of an issue, consider documenting it, and, if severe, withdrawing.
- Nevertheless, trying to work within a “family” system may be best where decision is to represent couple.
- Recognize clients have tough choices and act accordingly.

# Preparing for Initial Meeting

## How do blended family couples come to you?

- ***Preexisting*** relationship (personal or professional) with ***one*** partner but not other partner.
- ***Separate*** preexisting relationships (personal or professional) with ***each*** partner.
- ***No preexisting relationship*** with ***either*** partner.
- ***Beware: Any*** past relationship may potentially taint you.

(Technicalities rarely help those attempting to use them as shield.)

## How to handle initial fact-gathering meeting(s):

- Meet with **each** partner *separately*.
- Meet with *only one* partner.
- Meet with *both* partners *at same time*.
- Meet with *both* partners *together and separately*.

## Some may suggest:

- Meet with **both** partners, both ***separately and together***.
- Paul sometimes used a ***two-step*** engagement process where the first phase was to evaluate whether he could ethically represent the couple ***jointly***, while the second phase was the ***estate planning engagement***. You might do this on an initial call before the first consultation.
- May be best not to meet with ***just one*** blended family partner (unless you will only represent that one).

***(Risk of being perceived as biased in favor of partner with whom you met too great!)***

***(Also risk undue influence claim.)***

## Bottom line:

- Practice *defensively*, especially when representing blended family couples, **or** risk being sued or serving as unpaid fact witness.
- Unhappy clients are *more* likely to sue you, *more* likely to talk (and post) negatively about you, and *less* likely to pay *you*.

## Fears in Estate Planning

- In addition to fear of discussing or confronting their own **mortality** (called “**mortality salience**”), Paul has identified 12 distinct possible fears that clients can have in estate planning, especially in blended families, including:
  - Fear of estate planning **process**.
  - Fear of **estate planners**.
- **Result:** Clients procrastinate (“planning paralysis”).
- **Result:** Unforeseen results visited on blended families, particularly on couples not legally married.
- **Example:** Health care situation - patient lacks health care power of attorney/advance care directive. HIPAA and privacy rights might freeze the unmarried partner out.



**An analysis of the annual collection of non-tax estates and trusts litigation reported decisions reveals that a significant percentage of those cases involved blended families**

### **Why So Much Angst in Blended Families?**

- Divisions based upon divided loyalties.
- Children often grieving loss of parents' relationship.
- Children often grieving loss of deceased parent.
- Children stuck in "no one can replace Mama (or Daddy)."
- Children jealous of parent's new partner.
- Distrust of new partner's motives.
- **Result:** New partner and children often *fear* – despise – may be angry at-each other.

**Even in a subsequent union,  
there should not be extended back-and-forth  
negotiations, particularly through lawyers, over a  
marriage contract or property agreement.**

Why? May undermine foundation of couple's relationship.

Psychological counseling or coaching  
*"helps facilitate resolution of disagreements."*

*Leaving Money Wisely* by David W. Belin

- Few estate planners are schooled in psychological and emotional aspects of these discussions. (Goal should be a “win-win” for couple. Dr. Stephen Covey: *Seven Habits of Highly Effective People*.)
- **Problem:**
- Most lawyers/advisors see negotiations as **zero-sum games** in prenuptial agreements. (Wrong-headed in our opinion.)
- **Caution:**
- If the back and forth to resolve financial arrangements is significant, you should evaluate whether you should (can) continue to represent the blended couple **jointly** – this might be a sign to advise the parties to each obtain separate counsel, at least as to that issue.

# **Conflicts of interest** **and** **Ethical issues**

# Conflicts of Interest

- ***Conflict of Interest:*** This issue is much more vexing when it involves a blended family couple.
  - Conflicts of interest may become worse in ***hindsight***, after time has elapsed, than at time of engagement.
  - Be watchful for present ***actual*** conflicts of interest.
  - Be watchful for ***potential*** future conflicts of interest.

- ***Conflicts of interest = bad business***, even if the conflict doesn't rise to the level of an ethical problem for the estate planner.
- Conflicts of interest issues aren't confined to lawyers.
- We'll focus on conflicts of interest rules for lawyers, since they are well developed.
- **Note:** similar risks affect non-lawyers.

- ***Reminder:***
- The Model Rules of Professional Conduct (“MRPC”) for lawyers essentially restrict lawyers from representing people who are at odds with one another or who have issues in conflict with each other.
- Potential for ***divided loyalties*** is the reason for the rule.

## MRPC Rule 1.7:

### *General rule for conflicts for lawyers:*

Proscribes simultaneous representations of clients with “**concurrent conflict of interest**” *unless*

[1] lawyer *reasonably* believes that he/she can provide “**competent and diligent**” representation;

[2] it isn’t against law;

[3] matters don’t involve assertion of claim by one client against another in same proceeding before same tribunal; **AND**

[4] clients give “**informed consent**” - *in writing*.



- **“Concurrent conflict of interest” defined:**
- Representation of client **“*directly adverse*”** to another client OR (**this is big “or”**)
- **“*significant risk*”** that simultaneous representation will be **“*materially limited*”** by lawyer’s responsibilities to another client, former client or third person or by personal interest of the lawyer.”
- Can’t clients simply waive a conflict of interest in writing?

- MRPC Rule 1.0(e) defines “***informed consent***” and requires lawyer to communicate “***adequate information and explanation***” about “***material risks***” and “***reasonably available alternatives.***”
- Official comments to MRPC Rule 1.7 provide conflict must be “***consentable***” (i.e., some aren’t!).
- ***Consentable*** is circumstantial test under the comments-(not much help!).
- Might have to send clients to different lawyer just to explain conflict risks!

# Routine Modern Family Couple

## “Conflicts of Interest”:

- Classification of property as separate, jointly owned or as community property.
- *Smaldino* problem.
- Severing joint tenancies to allow for funding of credit shelter trust and separate funding.
- Waiver of spousal rights in retirement plan.
- Advising on applicability of spousal election.
- Breadth of powers of appointment.

## **Routine Modern Family Couple**

### **“Conflicts of Interest” (cont.):**

- Trust terms.
- Types of legacies and restrictions on legacies (trust v. outright) to spouses in general.
- Wealth disparities or economic dependence between partners.
- Interpretation of marriage contract or property agreement, including whether agreement would withstand attack.
- Legacies to children versus to partner.
- Waiver of reimbursement under IRC Sec. 2207A.

# Specific Blended Estate Planning Ethical Issues

# Traps of Joint Tenancies in Blended Family Couples

# Traps of Joint Tenancies in Blended Family Couples

- Joint tenancy can destroy an estate plan, and can really be what the client doesn't want, particularly in a blended family situation.
- In the context of a blended family, this almost always means that the children and other loved ones of the deceased joint tenant will get ***nothing*** with respect to that property, which often ***conflicts*** with the intentions of the deceased joint tenant.
- In many cases it may not be recommend that couples, particularly those in blended family relationships, own property as joint tenants for the above reason, and we certainly recommend highlighting ***the dispositive effects of joint tenancy, which can result in effectively disinheriting the descendants of the first joint tenant to die.***

# Traps of Joint Tenancies in Blended Family Couples

## Joint tenancy severances:

- What did the clients really understand/want?
- An estate planner who represents both partners **jointly** may have an ethical or a prickly client-relations problem with recommending severance of a joint tenancy arrangement. This is clearly an area of potential conflict between the partners.
- This potential for conflict is because joint tenancy may actually work in favor of a **younger** partner, particularly one who is less wealthy than the other partner, because the younger partner is actuarially more likely to survive and get all of that property.
- Nevertheless, we usually recommend **severance** of joint tenancies for blended family couples, reasoning that, in reality, you never really know who will survive (We've been fooled too many times).



# Traps of Joint Tenancies in Blended Family Couples

## Joint tenancy severances:

- One can sever a joint tenancy ***unilaterally*** without the other partner having to approve the change or even having to know about it.
- Again, this is a possible reason for clients to have ***separate*** representation by different lawyers, because an estate planner may be hamstrung by client relations or even ethical obligations to the other partner and unable to participate in severance without telling the other partner if the estate planner represents the couple (except in the rare circumstance where the estate planner represents each partner ***separately***).

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# Traps of Joint Tenancies in Blended Family Couples

## **Joint tenancy severances:**

- This secrecy might be a signal that the union is not that solid. You may want to ask the partner why he or she is feeling the need to act in secret.
- Perhaps it is justified because the other partner was asked and is being unreasonable. If that is how the partner sees it, ask them to consider for a moment what he or she would feel if the situation was reversed.
- Be careful in what you do.

# Traps of Joint Tenancies in Blended Family Couples

## **Joint tenancy severances:**

- If one of the partners still believes that he or she should go forward in secret, we strongly recommend encouraging them to consider the ramifications of their partner finding out that they've gone behind his or her back.
- Repeating – be careful.

# Gift-Splitting in the Context of Blended Family Couples

# Gift-Splitting in the Context of Blended Family Couples

- It is not unusual for one partner to have significantly more wealth than the other partner.
- Through what is known as *gift splitting*, the wealthier partner could make gifts of the entire amount, but, for gift tax purposes, it is as if both partners made the gifts, thereby doubling the gift.
- This technique only applies if the partners are legally married.
- Start by reading any prenuptial agreement to understand its terms.
- Gift splitting often is dealt with in a marriage contract, since IRC Sec. 2513 requires a consenting spouse to make an election to split gifts on a gift tax return (Form 709) and permits revocation of consent to split gifts. But IRC Sec. 2513 also requires that all gifts be split, which can create problems, particularly if gifts larger than annual exclusion gifts are contemplated.

# Gift-Splitting in the Context of Blended Family Couples

- Marriage contracts frequently require spouses to split ***all*** gifts made, to consent to the filing of a separate gift tax return and to agree not to revoke the consent, but this often is limited to ***annual exclusion*** gifts, although the gift-splitting tax rule applies to ***all gifts*** made in a calendar year.
- Therefore, if one spouse makes a large gift, the other spouse may be required to split the gift for tax purposes, but not be obligated under the marriage contract to split the gifts.

# Gift-Splitting in the Context of Blended Family Couples

- Because the election under IRC Sec. 2513(b) covers **all** gifts made during a calendar year, including gifts that exceed the annual exclusions that are available to the consenting spouse, thereby necessitating use of that spouse's lifetime gift tax exemption, a pre-nuptial agreement may compensate that spouse in some way for use of that applicable exclusion amount.
- This often is done through annual exclusion gifts to the children of the consenting spouse.
- But be certain to read and understand what the actual provisions, if any, provide for.



# Marriage Contracts and Property Agreements

# Marriage Contracts and Property Agreements

- Whether the couple has a marriage contract or property agreement. The possibilities include:
  - No agreement.
  - Agreement to be ***totally separate*** in property.
  - Agreement to keep ***separate property*** (and the income therefrom) separate, but otherwise have a community property regime.
  - Agreement that has aspects of any or all of the above, but which gives explicit detail as to what a partner is entitled to on split-up.

# Marriage Contracts and Property Agreements

- Marriage contracts and property agreements have become so common in blended family situations that they are almost the norm today—a corollary of the old adage “screw me once, shame on you; screw me twice, shame on me.”
- These types of agreements are attacked and broken often—given the higher incidence of dissolution in blended family couples, an estate planner must consider the agreement as subject to challenge.

# Marriage Contracts and Property Agreements

## What are the warning signs of a potentially unenforceable marriage contract or property agreement?

- Signed ***right*** before marriage ceremony.
- Betrothed ***not given sufficient time*** to review the marriage contract and/or to hire independent separate counsel to review and advise relative to the marriage contract.
- Significant ***economic disparity and economic dependence***.
- ***Age/education*** differences.

# Marriage Contracts and Property Agreements

- **Interpreting the marriage contract or property agreement:**
  - These agreements are some of the most ***hotly contested contracts in the law*** because of the emotions behind it.
  - If you didn't draft the marriage contract or property agreement (and sometimes even if you did), you will have to ***interpret and incorporate*** the estate planning related aspects of that agreement.
  - This is a potential source of conflicts of interest, whether you drafted it or not: if you didn't, your call may adversely impact your client; if you did, you might have some malpractice exposure.

# Marriage Contracts and Property Agreements

- Some of the more common estate planning provisions in marriage contracts or property agreements are:
  - In marriage contracts, ***waiver*** of the spousal election.
  - Grant of ***right to occupy*** property that one partner owns for a certain period of time or for the life of the other partner.
  - Agreement to maintain life insurance and to pay premiums on life insurance or annuities.
  - Agreement to maintain certain will or trust provisions, including income rights, fiduciary positions, etc.

# Marriage Contracts and Property Agreements

- Some of the more common estate planning provisions in marriage contracts or property agreements (cont.):
  - Agreement to waive spousal rights in retirement plans and IRAs. ***Retirement plans pose a prickly problem for blended family couples who are contemplating marriage.*** A nonparticipant spouse's interest in a community property retirement plan can't be devised or passed on if the nonparticipant spouse dies first- *Boggs v. Boggs*, 520 U.S. 833 (1997).
  - Careful description/delineation of tangible personal property owned by each partner.
  - Waiver of statutory rights to serve as fiduciary, PR, etc.
  - Agreement to consent to split gifts for federal gift tax purposes and to sign all necessary elections and returns to reflect the same.
  - ***Portability*** issues.

# Marriage Contracts and Property Agreements

- ***Common Complaints/Concerns when Considering Marriage Contracts:***
- Seen as an affront related to lack of trust in person and union – being treated as ***“gold digger.”***
- “What about me??” regarding security and hopes and dreams for ***“our”*** future nest-egg.
- Feeling forced and obliged – ***“having to”*** sign and not having a sense of choice.



# Lifetime Gifts/Transfers and Gift Tax Returns

- Under the current transfer tax structure, each individual is treated as a separate taxpayer who has to file separate transfer tax returns.
- If a spouse's gift tax return is audited, the other's gift tax return is not involved or affected by a subsequent adjustment.
- Likewise, if spouses are involved in a technique where there's a transfer from one spouse to the other, followed, as part of the same integrated plan, a transfer by the recipient spouse, there's a risk of the IRS asserting an indirect gift argument, a la Smaldino.

# Two Actual Cases on

# M**O**dern Family

# Issues

- *Sindell v. Gibson Dunn & Crutcher*, 54 Cal. App. 4th 1457 (2nd Dis. 1997).
- Husband and wife had separate **grown** children.
- Husband and wife were **separately** represented by counsel.

- Husband hired law firm to coordinate transfer of interests in closely held entity (his separate property) to his daughters.
- Lawyers advised: Gift and sell entity interests to children.
- Lawyers did ***not*** advise him to get consent/acknowledgment of separate property (which he had inherited) from his wife.

- Wife had *independent* wealth.
- Wife was represented by *separate* counsel.
- Three years later, after wife become incapacitated, her children sued step-father to nullify transactions, asserting transferred property was *community property*.

- A year after wife's children filed suit to nullify gift/sale on grounds that some transferred property was wife's community property, husband's children sued ***dad's*** lawyers for malpractice for failing to get wife's consent to and acknowledgment of gift/sale.

- Trial court dismissed husband's children's action against husband's estate planning lawyers as premature since there was no damage yet-because lawsuit by wife's children hadn't been concluded.
- Second District ***reversed***, holding the matter over for trial.

- Appellate court reasoned that damage in form of attorney's fees to **defend** against the action was damage in and of itself and remanded for trial.
- Case never reported again (Probably settled).
- Lesson: Even if **clearly** separate property (as seems to have been here), **get the waiver!**
- As the late Myron Cohen would say, "It couldn't hoit."



# Smaldino v. Comr., T.C. Memo. 2021-127 (Judge Thornton November 10, 2021)

- ***Mrs. Smaldino's Applicable Exclusion Amount:*** The practical effect of the Tax Court's opinion was to effectively ***negate*** any taxable gift as having come from Mrs. Smaldino by expressly holding that the taxable gift of units of Class B nonvoting interests in Smaldino Investments, LLC by Mrs. Smaldino roughly equal to her entire then applicable exclusion amount to the Smaldino 2012 Dynasty Trust ***one day after having received said gift from Mr. Smaldino*** to have actually been made ***indirectly*** to the Dynasty Trust by Mr. Smaldino.
- The gift was made in 2013, and the gift tax return was filed in 2014. The case was decided in 2021, long after the three-year gift tax statute of limitations had expired. And there's no applicable exclusion amount restoration mechanism.

# Smaldino v. Comr., T.C. Memo. 2021-127 (Judge Thornton November 10, 2021)

- ***Mrs. Smaldino's Applicable Exclusion Amount (cont.):***
- By virtue of the Tax Court's decision, what happens to Mrs. Smaldino's gift tax return and, specifically, to her complete use of her then applicable exclusion amount? Does Mrs. Smaldino ***automatically*** get her entire applicable exclusion amount restored?
- Clearly, Mrs. Smaldino's gift tax return wasn't at issue in this proceeding, and Mrs. Smaldino wasn't a party to the Tax Court litigation. As such, Mrs. Smaldino's gift tax return wasn't impacted by the decision. In our opinion, Mrs. Smaldino probably doesn't get her applicable exclusion amount restored unless she took some timely independent steps.

# Smaldino v. Comr., T.C. Memo. 2021-127 (Judge Thornton November 10, 2021)

- ***Ethics Issue:*** Did the same lawyer represent Mr. and Mrs. Smaldino jointly? The facts are not clear about whether the same lawyer represented both Mr. Smaldino and Mrs. Smaldino, and if he represented both of them, if he did so ***jointly*** or ***separately***.
- If the lawyer represented both of them, irrespective of the capacity, the lawyer might have a conflict of interest/ethics problem if the lawyer either recommended or advised the couple to engage in the transaction without pointing out the obvious risks to Mrs. Smaldino of the indirect gift exposure, which we believe should have been readily apparent to any competent estate planning lawyer, i.e., if the lawyer failed to apprise Mrs. Smaldino of the clear indirect gift risk of the scheme, in our opinion, the lawyer may have fallen below the standard of care.

# Smaldino v. Comr., T.C. Memo. 2021-127 (Judge Thornton November 10, 2021)

- Mrs. Smaldino purported to virtually exhaust her entire then applicable exclusion amount on the gift to the Dynasty Trust.
- Given the time that has elapsed, it may already be too late for Mrs. Smaldino to reclaim her applicable exclusion amount, suggesting some malpractice damage, although since Mrs. Smaldino is still living, it may be impossible to ascertain the damage.

# Smaldino v. Comr., T.C. Memo. 2021-127 (Judge Thornton November 10, 2021)

- And it's entirely possible that if Mrs. Smaldinoe dies with a total tentative estate (which would include her then applicable exclusion amount gift that she was unable to reclaim) of less than the federal estate tax applicable exclusion amount in effect at her death, then the tax element of the malpractice claim would be zero. However, are there other compensable damages?
- Arguably, under the theory articulated in *Sindell v. Gibson, Dunn & Crutcher*, 54 Cal. App. 4th 1457 (2nd Dis. 1997), the answer is yes, as an item of compensable damages would include Mrs. Smaldino's attorney's fees in investigating and pursuing the malpractice claim in the first place.
- Watch the ethical traps of **jointly** representing husband and wife in a transaction.

# For More Information About Estate Planning for Blended Families

- Marty and Paul did a three-session webinar series for Leimberg Information Services, Inc. [\[click link\]](#) “Estate Planning for Modern Families: Practical Advice for Practitioners, a Three-Part Webinar Series.”
- Paul recently published a book both for the lay audience and estate planners entitled *Yours, Mine & Ours: Estate Planning for People in Blended or Stepfamilies* (Paul Hood Services 2022), which is available at [Amazon](#) and all major booksellers.

# Conclusion

- Estate planning for clients who have blended or stepfamilies presents some of the greatest professional and ethical challenges for estate planners.
- We've just barely ***scratched the surface*** of the ethical quagmires, many of which are counterintuitive.
- In the immortal words of *Hill Street Blues* mythical Sergeant Phil Esterhaus, ***“Let's be careful out there!!!”***
- If you have questions, you can reach Paul at [paul@paulhoodservices.com](mailto:paul@paulhoodservices.com)
- Jonathan at [jblattmachr@pioneerwealthpartners.com](mailto:jblattmachr@pioneerwealthpartners.com) or
- Marty at [Shenkman@shenkmanlaw.com](mailto:Shenkman@shenkmanlaw.com)